TESTIMONY OF DAVID K. OWENS
ON BEHALF OF THE EDISON ELECTRIC INSTITUTE
BEFORE THE SUBCOMMITTEE ON ENERGY AND RESOURCES
COMMITTEE ON GOVERNMENT REFORM
U.S. HOUSE OF REPRESNTATIVES
JUNE 8, 2005

Mr. Chairman and Members of the Subcommittee:

My name is David K. Owens, and I am Executive Vice President of the Edison Electric Institute (EEI). EEI is the association of U.S. shareholder-owned electric utilities and industry affiliates and associates worldwide. We appreciate the opportunity to testify on electric reliability and transmission issues.

A Strong Transmission System Benefits Electricity Consumers

The U.S. electric system is comprised of an interconnected network of generating plants, transmission lines, and distribution facilities. Transmission lines carry electricity instantaneously over long distances from power plants to areas where it is needed. Reliable electric service and robust regional electricity markets depend on strong transmission systems.

A number of critical changes are needed now to encourage new transmission construction to meet the growing demands for electricity and to support regional wholesale markets. H.R. 6, the Energy Policy Act of 2005, which passed the House of Representatives in April, contains a number of important transmission reform provisions that would help to make our nation's transmission infrastructure stronger and more reliable. In the Senate, we are encouraged by recent committee action, and the prospect of floor action soon, on an energy bill that contains many of these same provisions. We

urge Congress to finally enact a comprehensive energy bill that addresses these issues as soon as possible this year.

Transmission: A Brief Legislative and Regulatory History

The Federal Energy Regulatory Commission (FERC) regulates rates for transmission of electricity in interstate commerce. States retain jurisdiction over rates for transmission used for retail sales by vertically integrated utility companies (those owning both power plants and power lines). The nation's transmission system has operated under this dual regulatory regime since the Federal Power Act was enacted in 1935.

When Congress passed the last comprehensive energy bill 13 years ago, one of the purposes of the electricity title was to encourage competition in wholesale electricity markets. Proponents believed that wholesale competition would benefit consumers through lower electricity prices. Since the Energy Policy Act of 1992, FERC has moved aggressively to foster wholesale competition by opening up the transmission grid to competitive electricity generators.

In 1996, FERC required utilities under its jurisdiction (basically shareholder-owned utilities) to provide open access to their transmission systems to all participants in wholesale electricity markets. In 2000, FERC issued a rule calling for voluntary formation of regional transmission organizations (RTOs) to control the operations of shareholder-owned utilities' transmission systems. These orders were intended to ensure that other players in wholesale markets could gain non-discriminatory access to shareholder-owned utilities' transmission lines to move their power to willing buyers.

The Transmission System Is Stressed

Our current transmission system was built primarily to ensure reliable, local electric service. It was not built to support competitive regional wholesale electricity markets that require moving large quantities of power across long distances.

The volume of actual transmission transactions has increased by 300 percent in the last five years. According to the North American Electric Reliability Council (NERC), transactions that could not be completed because of congestion on transmission lines increased almost eight-fold to more than 2,300 in 2004, compared with 300 uncompleted transactions in 1998.

EEI member companies, which own transmission as either vertically-integrated utilities, or as stand-alone transmission companies, are planning to make major investments in the nation's transmission infrastructure. But companies will not be able to follow through on those plans unless Congress enacts, and FERC implements, measures to help improve the investment climate by providing greater regulatory certainty.

From the mid-1970s through 1999, the growth in transmission investment did not keep pace with growth in the demand for electricity and capital additions in the generation sector. However, since 1999, we have seen signs of a reversal of this trend through growth in transmission investment by both vertically integrated companies and stand-alone transmission companies. For example,

- Annual transmission investment increased from $2.6 billion in 1999 to $3.6 billion[1] in 2000, $3.7 million in 2001, $3.8 billion in 2002, and $4.1 billion in 2003. Taken together, this represents a 12-percent annual growth rate over the period.

[1] Throughout this portion of this statement, all dollar values are expressed in constant 2003 dollars.

- Total circuit miles of high-voltage and extra-high voltage transmission lines (188 kV and above) owned and operated by shareholder-owned utilities increased 2.8 percent annually over the 1999-2003 period.
- In contrast, kWh sales of electricity from the nation's shareholder-owned electric utilities and affiliates to end-use customers increased only 0.7 percent annually over the same period.

This data confirms that the industry has begun to increase its transmission investment in excess of demand growth. However, to better understand whether this trend of increased investment will be sustained in the future, EEI members were recently asked to identify the level of planned transmission investment in their capital budgets over the 2004-2008 period.

The results show that member companies have preliminary plans to invest $28 billion over the 2004-2008 period, as compared to the $18 billion in recorded investment over the 1999-2003 period. Without question, shareholder-owned utilities are poised to make substantial investments in transmission infrastructure over the next five years. However, those investment plans are dependent upon greater legal and regulatory certainty. Congress must act now to help ensure these investment plans reach fruition.

While investment in transmission systems has begun to increase, the new transmission lines being built primarily are to help serve a utility's local customers and to connect new power plants to the grid. The level of investment in the long-distance, high-voltage wires that move electricity around and between regions of the country is not keeping pace with the growing demands being imposed on the system.

Significantly, the number of circuit miles of high-voltage and extra-high-voltage transmission lines (188kV and above) owned or operated by shareholder-owned utilities has grown by only 2.5 percent annually since 1999. These are the so-called "trunk line" facilities that are so critical for moving electricity around and between regions of the country. If these trends in transmission congestion and construction continue, they will inevitably undermine the consumer benefits of wholesale competition and could even render it more difficult to maintain the reliability of the system.

Transmission Reforms in H.R. 6, the Energy Policy Act of 2005

Reliable delivery of electricity to consumers remains paramount. And reliable electric service and robust regional electricity markets depend on strong transmission systems. H.R. 6, the energy bill passed by the House of Representatives, contains a number of important transmission reform provisions that would help to strengthen our nation's transmission infrastructure. These provisions include the following:

- **Mandatory Reliability Rules:** ***Establish mandatory reliability rules on all market participants, with FERC oversight.***

Today's electricity market requires a mandatory reliability system, with enforcement mechanisms. The August 2003 blackout was a dramatic reminder of the need for mandatory reliability rules.

The electric industry and the North American Electric Reliability Council (NERC) are addressing the immediate problems that led to the August 2003 blackout. These include:

  - Adding new audit programs;
  - Disclosing reliability violations and results of audits;

- Strengthening existing reliability standards and enhancing compliance with reliability rules;
- Improving operator training; and,
- Enhancing vegetation management practices around power lines.

The industry's actions are consistent with the recommendations of the U.S.-Canada Power System Outage Task Force, which studied the blackout and released its final report in April 2004.

All participants in wholesale electricity markets should be subject to mandatory, enforceable reliability standards that are developed or approved by an electric reliability organization, with oversight and enforcement by FERC. Since early 1999, a broad group of stakeholders, including EEI and many of its individual member companies, have supported legislation to achieve this goal. The version of the language that we support was in the energy bill conference report in the 108th Congress. We strongly urge the inclusion of these provisions in an energy bill, without the budget limitations contained in this year's House-passed version of H.R. 6.

- **Transmission Pricing Reform:** ***Require FERC to reform its transmission rate policy in a manner that will provide greater certainty to investment in the transmission system.***

Capital investments in upgrades and new transmission lines must increase to help strengthen the transmission grid. Furthermore, increased transmission investment can help reduce electric bills.

We believe that FERC and the states should utilize innovative transmission pricing incentives to attract the capital necessary to fund needed investment in transmission. Transmission pricing should (1) allow for cost recovery of fixed and

variable costs and a reasonable return on transmission investment; (2) eliminate the pancaking of rates within a regional transmission organization (RTO) region; (3) ensure that cost responsibility follows cost causation; (4) minimize the potential for cost shifting; (5) permit the recovery of all prudently incurred transition costs, and (6) promote efficient siting of new transmission and generation facilities.

We support the FERC pricing and transmission technologies provisions in H.R. 6, particularly incentives to expand transmission infrastructure, such as the recovery of costs for planning and pre-certification of transmission facilities and the recovery of costs through construction work in progress for transmission facilities. While some of these incentives are targeted specifically to transmission providers that participate in RTOs, we believe their benefits should be expanded to include all transmission providers. Likewise, we encourage the states to assure that utilities can recover their costs for investments for transmission under state regulation, with a reasonable rate of return.

According to a December 2001 FERC "Electric Transmission Constraint Study," transmission costs make up only 6 percent of the current average monthly electric bill for retail consumers. On the other hand, generation costs make up 74 percent of the average bill. By reducing transmission congestion, investments in new transmission will allow greater use of lower cost generation.

FERC estimates that a 20-percent increase (or $12.6 billion) in transmission investment would add only *87 cents* to an electric customer's average monthly bill. But, since increased transmission investment will help reduce congestion and enable lower cost power to reach consumers more easily, FERC anticipates that the net benefits to overall electric bills could be potentially quite large.

For example, FERC estimates that if the reduced transmission congestion resulted in just a 5 percent savings in generation costs, consumers would see more than a $1.50 decrease in their average monthly bills. If the generation savings from reduced congestion were 10 percent, the average monthly bill for consumers would drop by $4.00. So, a small increase in transmission investment can reap a much more significant benefit in lower generation costs.

In addition to investments to relieve congestion, investments in new technology to help improve the control and use of existing transmission lines are critically important to promote reliability.

In addition to assuring cost recovery, transmission pricing reform should assure that those who cause transmission investments are responsible for their costs. The energy bill conference report in the 108th Congress contained another very important transmission rate reform to assure that entities that cause transmission costs to be incurred will help bear their fair share of those costs. While not included in H.R. 6 this year, the "voluntary transmission pricing plans" section of last year's conference report recognized "participant funding" plans could pay for transmission upgrades and expansions so that transmission providers who are not currently members of RTOs or ISOs would have the same pricing flexibility that FERC allows in those organized markets. We support the inclusion of participant funding language in the final version of the energy bill in this Congress to provide an important option for transmission construction.

- **FERC Backstop Siting Authority:** ***Give FERC very limited backstop transmission siting authority to help site transmission lines in Department of Energy (DOE)-designated "national interest electric transmission corridors" if the proposed transmission line is consistent with the public interest and a state***

lacks the authority to site the transmission line or is unwilling to site the line within a certain time period.

Regional electricity markets require a transmission siting process that has the ability to consider regional and even national needs. FERC has jurisdiction over rates for interstate transmission and wholesale electricity markets, but it currently does not have any authority over transmission siting to help ensure that there is sufficient transmission capacity to support those markets.

Even though transmission lines and natural gas pipelines serve essentially the same purpose – to move large amounts of energy across long distances – their siting processes are very different. Congress has given FERC the authority to site interstate natural gas pipelines, but individual states have jurisdiction over siting transmission lines. EEI would prefer that FERC be given transmission siting authority equal to its authority to site natural gas pipelines, but Congress should, at the least, give FERC limited backstop siting authority to get the most critically needed transmission lines built in certain areas.

While traditional state siting processes will be adequate for most local upgrades to existing transmission systems, limited FERC backstop siting authority could be a critical aid in developing the more significant transmission infrastructure needed to support regional wholesale electricity markets. That's because most state siting laws do not recognize the role new entities, such as multi-state RTOs or independent transmission companies, will play in transmission planning and siting. In many states, these new entities are not even considered utilities under state laws and, therefore, are not eligible to obtain the necessary permits from states to build new transmission.

Before states will grant utilities siting permits, utilities typically must prove that the new facilities are needed. The determination of "need" often focuses on service to in-state consumers. Most state siting laws do not allow for the consideration of regional, or out-of-state, benefits of new transmission lines. If states consider only intrastate benefits and not regional benefits, they may have little choice under state law but to reject the proposed line, even if the benefits to the region are significant.

FERC has decades of experience in siting energy facilities. Since 1948, interstate natural gas pipelines have gone to FERC for certificates that grant them eminent domain authority. Hydroelectric developers have used this federal permitting process since 1920. Protection of the environment is a top consideration in FERC's processing of natural gas pipeline certificates. Under the National Environmental Policy Act, FERC is required to perform a comprehensive environmental analysis of all gas pipeline construction proposals. H.R. 6 as passed by the House would require the same environmental protection process for any transmission line construction proposal.

H.R. 6 would give FERC very limited backstop transmission siting authority. This authority extends only to helping site transmission lines in "interstate congestion areas" designated by the Department of Energy (DOE) and only if states have been unable to agree or act within a year. We strongly urge its inclusion in the final energy bill.

- **Federal Permitting Reform:** ***Reform the transmission permitting process on federal lands by designating DOE as the lead agency to coordinate and set deadlines for the federal environmental review and permitting process.***

The unnecessarily complicated, time-consuming and difficult multi-jurisdictional federal permitting process to site energy facilities is another major impediment to building new transmission. It may be even worse for transmission facilities than any

other energy project because long transmission facilities often cross federal lands within the jurisdiction of many different agencies and bureaus that simply do not coordinate well with each other. In some areas of the country, this is the principal impediment.

Problems with the federal permitting process include (1) a severely fragmented process, where each federal agency with potential jurisdiction has its own set of rules, timelines for action and processes for permitting; (2) the tendency by federal agencies to require multiple and duplicative environmental reviews; (3) a failure to coordinate with any state siting process; and (4) a lack of harmonized permit terms from one agency to the next.

The federal transmission permitting process needs to be coordinated, simplified and made to work with any state siting process. H.R. 6 accomplishes this objective by designating DOE as the lead agency to coordinate and set deadlines for the federal environmental and permitting process. In addition, DOE would be responsible for coordinating the federal process with any state and tribal process. A state where a transmission facility would be located could appeal to DOE when a federal decision deadline has been missed or a federal authorization has been denied. To further facilitate siting, the bill sets deadlines for the designation of transmission corridors across federal lands. We strongly support these provisions.

- **"FERC Lite":** ***Ensure that all transmission providers must allow open access to their transmission lines to any third-party wholesale power seller.***

Government-owned utilities and electric cooperatives collectively own and operate about 32 percent of the nation's transmission system, but in some regions that figure is much higher.

In the Pacific Northwest, the federal Bonneville Power Administration (BPA) alone owns and controls nearly three-quarters of the region's high-voltage transmission capacity. The entire state of Nebraska and most of Tennessee are served by utilities that are not regulated by FERC, yet they are integrated into a multi-state transmission grid.

These transmission owners are not subject to the same level of FERC jurisdiction over transmission that applies to shareholder-owned utilities. As previously mentioned, under a 1996 rule (Order No. 888), FERC requires all shareholder-owned utilities to provide non-discriminatory open transmission access to any third-party wholesale power seller.

According to a December 2002 GAO report, "Lessons Learned From Electricity Restructuring," because of FERC's lack of jurisdiction over government-owned utilities and electric cooperatives

> FERC has not been able to prescribe the same standards of open access to the transmission system. This situation, by limiting the degree to which market participants can make electricity transactions across these jurisdictions, will limit the ability of restructuring efforts to achieve a truly national competitive electricity system and, ultimately will reduce the potential benefits expected from restructuring.

We believe that this bifurcated regulation of interstate transmission lines is ultimately unsustainable as the industry's structure continues to evolve. The nation's transmission grid is physically integrated. Electrons do not recognize boundaries between public and private transmission ownership.

We believe sound public policy to protect consumers would mean putting all utilities participating in interstate wholesale electricity markets under FERC's full "just

and reasonable" requirements. At a minimum, EEI's member companies strongly support inclusion of an effective "FERC lite" provision in any electricity bill.

The "FERC lite" provisions of H.R. 6 would impose only open-access requirements on a limited basis, and only in the wholesale market. They would not force government-owned and cooperative utilities to open up their systems to retail competition. Nor would these provisions subject them to any other FERC requirements imposed on shareholder-owned utilities in wholesale markets.

- **Federal RTO Participation:** ***Clarify federal law to authorize federal utilities to join an RTO or independent transmission system operator (ISO) voluntarily.***

We believe it is essential to eliminate any legal uncertainty about whether federal utilities can delegate authority over their transmission systems to a RTO. In the Pacific Northwest, it will be impossible to form a successful RTO without participation by the Bonneville Power Authority. Federal utility participation is important to RTO formation in other regions as well. H.R. 6 includes a provision that explicitly authorizes federal utilities to join RTOs.

- **PUHCA Modernization:** ***Repeal and modernize the Public Utility Holding Company Act (PUHCA) to help attract significant amounts of new investment capital to the industry, which will help strengthen the transmission infrastructure.***

We also believe that repealing PUHCA will help attract significant amounts of new investment capital to the industry. By imposing limitations on investments in the regulated energy industry, PUHCA acts as a substantial impediment to new investment in energy infrastructure, keeping billions of dollars of new capital out of the industry. As a result, we believe that this outdated statute has contributed to the failure of the electricity

infrastructure to keep pace with growing electricity demand and the development of regional wholesale markets.

PUHCA imposes outmoded restrictions on the business activities of electric and gas utility holding companies and acts as a barrier to efficient competition. Furthermore, it prevents consumers from reaping the economic and efficiency benefits that can accrue from having access to products and services offered by companies of national scope and scale.

For instance, under PUHCA, a registered holding company must confine its operations to a "single integrated public utility system" (with certain exceptions) located in a "single area or region" of the country. This outdated "physical integration" requirement prevents utility companies from investing capital outside their geographic region, shutting off a valuable potential source of domestic capital investment in needed energy facilities and, ironically, fostering the very kind of concentration in regional energy markets that FERC is trying to reduce.

Even without PUHCA, utility customers and investors are protected. Retail customers are protected fully by state regulation or oversight of retail electric service, and wholesale customers are protected by FERC oversight and regulation. Utility companies have long been, and will continue to be, among the most heavily regulated businesses there are.

H.R. 6 contains provisions that would repeal PUHCA and transfer consumer protections to FERC and the states. These provisions are similar to PUHCA repeal language that has been included in every major electricity bill considered by Congress over the last decade, and which have been endorsed by every Administration—

Republican and Democratic—since 1982. They should be included in the energy bill again this year.

- **Accelerated Depreciation:** ***Provide for enhanced accelerated depreciation for electric transmission assets, reducing the depreciable lives from 20 to 15 years, similar to the tax treatment governing other major capital assets.***

The U.S. tax code should be amended to provide enhanced accelerated depreciation (from 20 to 15 years) for electric transmission assets, similar to the tax treatment governing other major capital assets. Currently, transmission assets receive less favorable tax treatment than other critical infrastructure and technologies. Accelerated depreciation for transmission will help increase investment in, and strengthen, our energy infrastructure.

Conclusion

Congress needs to finish the job and pass an energy bill as soon as possible to help promote fuel diversity, improve energy efficiency and conservation, provide regulatory certainty in energy markets, and encourage investment in critical energy infrastructure. We urge Congress to adopt an energy bill that includes the transmission provisions contained in H.R. 6.